ASSEMBLY

30 MARCH 2011

REPORT OF THE CORPORATE DIRECTOR OF FINANCE AND RESOURCES

Title: 2011/12 Treasury Management Strategy	**For Decision**

Summary

This report deals with the Treasury Management Annual Investment Strategy Statement, Treasury and Prudential Indicators, Annual Investment Strategy and borrowing limits, in compliance under section 15 (1) (a) of the Local Government Act 2003.

The production and approval of a Treasury Management Annual Strategy Statement and Annual Investment Strategy are requirements of the Council under Section 15(1) of the Local Government Act 2003. It is also a requirement of the Act to set an authorised borrowing limit for the forthcoming financial year.

The Local Government Act 2003 also requires the Council to have regard to the Prudential Code, and to set prudential indicators which take into account the Council's capital investment plans for the next 3 years.

Wards Affected: All

Recommendation(s)

The Assembly is asked to consider and approve the Treasury Management Strategy Statement for 2011/12 (this document), and within this document the following:

1. The current treasury position for 2010/11 and prospects for interest rates:

2. The Authorised borrowing limit of £257m for 2011/12, which will be the statutory limit determined by the Council, pursuant to section 3(1) of the Local Government Act 2003;

3. The Borrowing Strategy, Borrowing Requirement Strategy, Borrowing Requirement Debt Rescheduling Strategy and Policy on borrowing in advance of need for 2011/12;

4. The Minimum Revenue Policy Statement for 2011/12 which sets out the Council's policy on repayment of debt;

5. The Annual Investment Strategy and creditworthiness policy for 2011/12 (Appendix B), which outlines the investments that the Council may use for the prudent management of its investment balances. It also includes details of benchmarks set for external managers. The power is delegated to the Chief Financial Officer to change these benchmarks as required;

6. The Treasury Management Indicators and Prudential Indicators for 2011/12 (Appendix A);

7. Treasury Management Principles, areas of responsibility and frequency as required by the Revised Code of Practice for Treasury Management 2011/12(Appendix C) as well as the key reporting requirements as required by the Code (Appendix D); and

8. The Housing Reform and effects on treasury management Housing Revenue Account Reform and Impact on Treasury Management.

Reason(s) It is necessary for the Assembly to approve this report due to the requirements of the Local Government Act 2003.

Comments of the Chief Financial Officer

The aim of this Treasury Management Strategy is to maximise the Council's financial resources. Detailed financial considerations are considered throughout this document.

Comments of the Legal Partner

Local authorities have power to borrow and invest under sections 1 and 12 Local Government Act 2003 for any purpose relevant to their statutory functions or for the purposes of the prudent management of their financial affairs. The Council is required under the 2003 Act to have regard to any relevant guidance. In this regard the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 (as amended by the Local Authorities (Capital Finance and Accounting) (England) Regulations 2010 require local authorities to have regard among other things to the Prudential Code for Capital Finance in Local Authorities and Treasury Management in the Public Services Code of Practice and Cross Sectoral Guidance Notes.

This report sets out a proposed strategy for investment in accordance with the legislation and codes of practice referred to. Members will note that the strategy includes an element of borrowing. In relation to borrowing, section 3 Local Government Act 2003 requires local authorities to determine and review how much it can afford to borrow (the affordable borrowing limit). The proposed level of borrowing is within the authorised limit. In relation to capital projects local authorities are also required to charge to a revenue account a minimum amount (minimum revenue provision) for that financial year and may charge any amount in addition to the minimum in respect of the financing of capital expenditure incurred by the local authority (Local Authorities (Capital Finance and Accounting) (England) Regulations 2003) (as amended).

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1. Treasury Management Strategy for 2011/12

1.1 The Local Government Act 2003 (the Act) and supporting regulations require the Council to 'have regard to' the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.

1.2 The Act therefore requires local authorities to set out their treasury strategy for borrowing and to prepare an Annual Investment Strategy (as required by Investment Guidance issued subsequent to the Act). This sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

1.3 The Department of Communities and Local Government (CLG) has issued revised investment guidance which came into effect from 1 April 2010, and the Council has adopted the recommendations of the guidance.

1.4 The 2011/12 strategy covers:

- The treasury limits in force limiting treasury risk, treasury and prudential indicators;
- The current treasury position and borrowing position;
- Prospects for interest rates;
- The Borrowing Strategy and Borrowing Requirement;
- The policy on borrowing in advance of need and debt rescheduling strategy;
- The Minimum Revenue Provision strategy;
- Housing Revenue Account Reform and Impact on Treasury Management
- The Annual Investment Strategy and Investment Policies;
- Security of Capital and creditworthiness policy;
- Statutory Requirements on Reporting of Treasury Management;

2. The Balanced Budget Requirement

It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the Council to produce a balanced budget. In particular Section 32 requires a local authority to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This means that increases in capital expenditure must be limited to a level whereby charges to revenue caused by borrowing and any increases in running costs are limited to a level which is affordable within the projected income of the Council for foreseeable future. This is confirmed in the Council Tax report.

3. Treasury Management Policy Statement

3.1 The Council defines its treasury management activities as “The management of the authority’s investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks”.

The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation.

4. Treasury Limits and Indicators for 2011/12 to 2013/14

4.1 It is a statutory duty under section 3 of the Local Government Act 2003 and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow. The ‘Authorised Limit’ represents the legislative limit specified in the Act.

4.2 It is proposed that the ‘Authorised Limit’ increase to £257million for 2011/12, £281m for 2012/13 and £291m for 2013/14. The Council must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires it to ensure that total capital investment remains within sustainable limits and in particular that the impact upon its future council tax and council rent levels is ‘acceptable’.

4.3 The 2011/12 – 2014/15 capital programme report that is also being considered on this agenda is proposing a total capital programme that will have an underlying borrowing requirement of around £207m by the end of 2013/14. This does not include the funding of decent homes as the government has not provided final figures nor does it include the borrowing to finance the HRA reform.
As this is a legal limit, sufficient headroom has been provided to ensure that any major capital investment projects where financing has yet to be finalised, are not restricted by this statutory limit. This limit covers any short term borrowing for cashflow purposes as well as long term borrowing for capital projects, finance leases, PFI initiatives as well as any unforeseen incidences where expected capital receipts are not forthcoming due to unexpected economic factors.

Full details of the Council’s Treasury Indicators have been included in **Appendix A** to this document. The Council adopted the revised 2009 CIPFA Prudential Code of Practice in February 2010.

5. Current Portfolio Position

5.1 Investments and borrowing balances

The table below shows the Council’s current Rate of Return at 31 December 2010:

	31 December 2010		Average rate of return/payment
	£'000		%
Borrowing			
Fixed rate funding - PWLB	30,000		4.06
Variable rate funding - Market Loan Market Loan	20,000 20,000		3.98% 4.15%
		70,000	
Other long term liabilities		25,904	
Gross Debt		**95,904**	
Investments			
Council in House Team	51,194		1.15%
Scottish Widows	11,400		1.28%
Investec Asset Management	28,219		1.39%
Royal Bank of Scotland (RBS)	15,000		0.74%
Total Investments		105,813	
Net debt		**9,909**	

Current and Projected Portfolio Position

	Current Portfolio £'000	2010/11 Estimate £'000	2011/12 Estimate £'000	2012/13 Estimate £'000	2013/14 Estimate £'000
External borrowing:					
Fixed rate PWLB	30,000	50,000	70,000	80,000	90,000
Fixed rate Market	0	0	0	10,000	10,000
Variable rate PWLB	0	20,000	40,000	50,000	50,000
Variable rate market	40,000	40,000	50,000	50,000	55,000
Total External borrowing	70,000	110,000	170,000	190,000	205,000
IFRS Long Term Liabilities:					
PFI	25,262	32,960	38,595	26,674	23,818
Finance Leases schools	642	601	473	251	39
Finance Lease Vehicles	0	0	10,000	10,000	10,000
Total Gross External Debt	95,904	143,561	219,068	226,925	238,857
Total Investments	105,813	96,720	90,555	91,913	94,211
Net Borrowing Position/ Net Investment Position	9,909	(46,841)	(128,513)	(135,012)	(144,646)

5.2 The sum invested broadly represents the reserves, provisions and balances that the Council holds together with the impact of any difference between the collection of income and expenditure (working capital). From 1 April 2011, the pension fund cash currently managed by the Council will no longer be reported as part of the Council's balance. As at 31 December this sum was £16m.

6. Prospects for Interest Rates

6.1 The level of, and fluctuations in interest rates, are a key consideration for any treasury management strategy. In 2010/10, bank rate remained unchanged. This position is expected to change by Q3 2011/12 with expectations tending towards a further 1.0% increase in the later part of 2012 and 2% increase in 2013/14.
The Council has ensured that sufficient provision has been made in the Medium Term Financial Strategy to cover reduction in income for 2011/12 should interest rates fail to rise.

The Council invests its portfolio throughout the year, and the level of interest rates determines the interest receipts that are generated to support ongoing revenue expenditure. The Council has set it budget based on a return of 1.50%. In order to meet this target, the Council will avoid locking into longer term deals while investment rates are expected to begin to rise.

6.2 There is a downside risk to any forecast provided for 2011/12 if the recovery from the recession proves to be weaker and slower than currently expected. To arrive at an expectation of interest rates for 2011/12 and beyond, a number of judgements and assumptions are made; in addition this involves a high degree of uncertainty.

6.3 The Council has appointed Sector Treasury Services as treasury adviser to the Council. Part of the service provided assists the Council in formulating a view on interest rates.

The table below draws together a number of current City forecasts for short term, variable and longer fixed interest rates.

	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13
Bank rate	0.5%	0.5%	0.75%	1.00%	1.25%	1.50%	2.0%	2.25%	2.25%
3 month LIBID	0.70%	0.80%	1.00%	1.25%	1.55%	1.75%	2.00%	2.25%	2.50%
6 month LIBID	1.00%	1.10%	1.20%	1.50%	1.80%	2.10%	2.40%	2.60%	2.80%
12 month LIBID	1.50%	1.60%	1.80%	2.10%	2.40%	2.70%	3.00%	3.10%	3.20%

7. Borrowing Strategy and Borrowing Requirement

7.1 The decision to borrow is a treasury management decision and is taken by the Corporate Director of Finance & Resources under delegated powers of the Council's constitution. The key objective of the Council's borrowing strategy is to secure long term funding for capital projects at borrowing rates that are as low as possible.

7.2 The Council's borrowing strategy will give consideration to the following when deciding to take up new loans:

- Use internal cash balances while the current rate of interest on investments remains at an all time low. However consideration will also be given to weighing the short term advantage of internal borrowing against potential long term costs if long term borrowing rates begin to increase more than forecast.
- Using Public Works Loan Board (PWLB) variable rate loans
- Using long term fixed rate market loans where rates are significantly less than PWLB rates for the equivalent maturity period.
- Maintain an appropriate balance between PWLB and market debt in the debt portfolio
- Use short dated PWLB fixed rate loans where rates are expected to be significantly lower than rates for longer period. This ensures that the maturity profile of the Council's debt portfolio is well spread.
- Ensure that new borrowing is timed at periods when rates are expected to be low.
- Consider the issue of stocks and bonds if appropriate.

7.3 The Council's borrowing requirement is as follows:

Capital Financing Requirement (CFR)	2011/12 £'000 Estimate	2012/13 £'000 Estimate	2013/14 £'000 Estimate
Housing Revenue Account (HRA)	(3,952)	(3,952)	(3,952)
General Fund	210,175	226,161	239,045
Total CFR (borrowing requirement)	206,222	222,209	235,093

7.4 The borrowing rate forecast for 2011/12 from Sector is as follows:

	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12
Bank rate	0.5%	0.5%	0.75%	1.00%	1.25%	1.50%	2.00%	2.25%
5yr PWLB rate	3.70%	3.70%	3.70%	3.80%	3.90%	4.00%	4.10%	4.20%
10yr PWLB rate	4.90%	4.90%	4.90%	4.90%	4.90%	5.00%	5.10%	5.20%
25yr PWLB rate	5.40%	5.40%	5.40%	5.40%	5.40%	5.50%	5.50%	5.50%
50yr PWLB rate	5.40%	5.40%	5.40%	5.40%	5.40%	5.50%	5.50%	5.50%

7.5 Sensitivity of the forecast

The Council will continually monitor interest rates and market forecasts and would seek advice as required. In instances when there is significant risk of a sharp fall in long and short term rates for example at times of market recessions or risks of deflation then the Council may decide to postpone long term borrowing or reschedule its current debt portfolio. At times when rates rise significantly sharper than current forecast, the Council will re-appraise its debt portfolio with the likely action that fixed rate funding may be withdrawn whilst interest rates were still relatively cheap.

7.6 External and Internal Borrowing

The revised Prudential Code paragraph 43 now requires each authority to explain its policy on gross and net debt, where there is a significant difference between them.
Comparison of gross and net debt positions at year end

	2009/10	2010/11	2011/12	2012/13	2013/14
	Actual	Probable outturn	Estimate	Estimate	Estimate
	£'000	£'000	£'000	£'000	£'000
Actual Loans (gross)	70,000	110,000	170,000	190,000	205,000
Cash Balances	115,889	96,720	90,555	91,913	94,211
Net Cash (debt)	45,889	(13,280)	(79,445)	(98,087)	(110,789)

- The Council during the financial year will carefully consider the difference between borrowing rates and investment rates to ensure that the Council obtain value for money.
- Low bank rates are still expected for most of 2011/12 and 2012/13 in comparison to external borrowing rates. This means the Council will continue to utilise internal borrowing rather than external borrowing as the opportunity arises.

- Short term savings as a result of avoiding new long term external borrowing in 2011/12 will also be considered in conjunction against the potential for incurring additional long term extra costs. In some instances the Council may delay unavoidable new external borrowing until later years when PWLB long term rates are forecast to be significantly lower.

8. Borrowing in Advance of need and Debt Rescheduling Strategy

8.1 The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance of need will be considered carefully by the S151 Officer to ensure that this is in line with the financing of the capital programme (the “capital financing requirement”), that value for money can be demonstrated and that the council can ensure the security of such funds.

In coming to a decision whether borrowing will take place in advance of need the Council will:

- ensure that there is a clear link between the capital programme or Housing Revenue Account Reform and maturity profile of the existing debt portfolio which supports the need to take funding in advance of need;
- ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered;
- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow;
- consider the merits and demerits of alternative forms of funding; and
- consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use.
- consider the impact of counterparty and other risk which may arise as a result of increased cash balances from borrowing in advance of need,

8.2 The key decision in debt restructuring will be the ability to demonstrate value for money. The decision to reschedule will be taken by the S151 Officer under delegated powers of the Council’s constitution and in consultation with the Council treasury management advisers.

8.3 Due to the short term borrowing rates being expected to be cheaper than long term rates, there are likely to be significant opportunities to generate savings by switching from long term debt to short term debt. However these savings will be considered in light of their short term nature and likely cost of refinancing these short term loans once they mature. The Council is aware that any such rescheduling and repayment of debt is likely to cause a flattening of the Council’s maturity profile. The Council will consider restructuring its debt if:

- there will be cash savings from the exercise
- there is a need to amend the maturity profile of its portfolio
- if it needs to borrow in advance of need
- if it decides to pay some of its debt prematurely

9. Housing Revenue Account and Impact on Treasury Management

9.1 Following two earlier Consultation papers issued by the previous government, a modified self-financing system is to be introduced on 1 April 2012. This is the most fundamental reform of housing finance since 1989. It is anticipated that the self-financing basis of the reforms will be mandatory for all housing authorities from the implementation date, 1 April 2012, and final debt settlement amounts will be issued by CLG in January 2012.

The fundamental aspect of the Reform is the replacement of the present Housing Revenue Account Subsidy system with a self-supporting system under which there will be no on-going support from central government.

The government will achieve the abolition of existing positive and negative subsidy situations by adjusting existing debt liability levels so that authorities will, in general, have an increase or decrease in their debt.

CLG state that self-financing will require local authorities to have a long term business plan which includes the costs of borrowing and estimated movements in interest rates. Such matters will therefore influence the nature of treasury management practices to be adopted.

Authorities like this Council that are participating in the National Affordable Housing Programme by developing new housing for social rent outside of the HRA subsidy system will not be penalised.

It is anticipated that the ring-fence between the HRA and the General Fund will stay and most debit/credit principles that are presently incorporated within the Item 8 Determination, such as debt management costs and PFI scheme payments will remain.

9.2 From a treasury management viewpoint, the reforms involve two entirely different issues:

1. On the debt settlement date, authorities will be either required to make a payment to CLG or will qualify for a capital receipt from the CLG.

2. During the course of 2012/13, authorities which had a positive HRA CFR on 1 April 2012 will need to consider whether their borrowing or alternative form of finance should either:

   a) be disaggregated in order to create separate HRA and Non-HRA borrowing pools, or
   b) determine how the HRA should in future be recharged in respect of its share of debt financing costs.

9.3 On the debt settlement date it is anticipated that as the Council's HRA has very little debt, the Council will fall into the CLG category 2 – Authorities with an existing borrowing/debt liability who are required to make a payment to CLG and receive allocation of additional HRA debt liability and new borrowing. Such authorities will take on an additional HRA debt liability, which they have discretion to decide as to the means of funding.

In view of anticipated changes in interest rate levels by the debt settlement date, the use of advance borrowing may be considered appropriate or prudent. However, under present HRA Determination Rules, this is likely to cause an increase in the proportion of debt financing costs borne by the General Fund (the cost of carry). It is expected that the Council like others will make representations to CLG to facilitate forward borrowing in a manner which allows for this to be accompanied by HRA Item 8 charge increases coupled with associated subsidy cover.

9.4 It is on this basis that the Council anticipates HRA borrowing requirement of around £237m. In order to facilitate borrowing in advance of need when interest rates facilitate this, a revised Authorised Limit for 2011/12 will be submitted to the Assembly for approval. Associated Prudential Indicators and further borrowing in advance of need policy is currently being reviewed against the 2012/13 treasury management strategy.

9.5 The review will include:

- disaggregating of HRA proportion of existing borrowing and separation of all new borrowing.
- ensuring that all new borrowing after the settlement date should be related to either GF or HRA.
- internal borrowing is properly identified between GF and the HRA while relying on CIPFA's assumption that internal borrowing has been facilitated by the availability of largely GF balances and reserves.
- The HRA recharge is made in the most equitable manner and would be carried out as part of the interest on balances calculation that is made at present.

10. Minimum Revenue Provision (MRP) Strategy

10.1 With effect from 1 April 2008, local authorities are required to make a 'prudent provision' for repayment of debt having regard to the statutory guidance issued by the Department for Communities and Local Government.

The MRP on expenditure financed by borrowing under Supported Capital Expenditure is 4% of that expenditure. The MRP on expenditure financed by borrowing that is unsupported is calculated using the Equal Installment Method, i.e. the borrowing is written down over the life of the asset that it financed. The MRP for the PFI scheme is equivalent to the capital repayment required.

11. Annual Investment Strategy and Investment Policies

11.1 Security of capital and liquidity of its investments are the Council's key investment priorities. However the Council will aim to achieve optimum returns on its investments after careful consideration of level of security and liquidity. Counter party ratings will not be lowered in order to optimise return on investments. Borrowing of monies purely to reinvest is unlawful, the Council will not engage in such activities.

11.2 Investment instruments identified for use in the financial year are listed in Appendix B to this report. Under the requirements of the Investment Guidance issued by the Department for Communities and Local Government, investments need to be classified into specified and non-specified. The Annual Investment Strategy states which investments the Council may use during the financial year. It is a requirement to report these investments to the Assembly for approval. It is the delegated responsibility of the S151 Officer to determine the exact instrument to use within these classifications.

11.3 The Council will maintain a mixed portfolio of investments in 2011/12. Where the maximum returns can be achieved and on the advice of our advisers, we may seek to invest in structured investment products and money market funds. Gilts investments will continue to remain on a segregated basis.

11.4 The monitoring of counterparties will be kept under continuous review.

11.5 Funds managed by the in-house team are a mix of cash flow derived balances and core balances. The Council will avoid locking into longer term deals while investment rates are down at historically low levels or when rates are expected to rise except when attractive rates with counterparties of high credit worthiness become available within risk parameters set by the Council.

11.6 External cash managers have been set the following challenging benchmarks for 2011/12.

Fund Manager	2011/12 Benchmark	Reason
• Investec Asset Management • Scottish Widows (SWIP)	1.50% (or 3 month LIBID, whichever is higher) 1.50%, (or 3 month LIBID, whichever is higher)	• Bank Rate now 0.5% as at February 2011 • Bank Rate Forecast to increase by 0.5% and expected to increase to 1.0% in Q3 of 2011 and 1.5% after. • Consideration given to restrictions in counterparties • Maximising of Council's return on investments at minimal risk • Maximisation of the Council's returns in order to meet budget pressures

The power to change benchmarks as above is delegated to the Chief Financial Officer.

11.7 The Council may permit its external fund managers and officers to use instruments such as gilts, bonds, pooled funds, callable investments and other longer-dated instruments. Limits will have to be established in the use of such instruments to ensure that the Council can have access to its investments. These Treasury Management limits can be set as either a £ amount or percentage.

11.8 Provisions for Credit-related losses

If any of the Council's investments appeared at risk of loss due to default, (i.e. a credit-related loss and not one resulting from a fall in price due to movements in interest rates) the Council will make revenue provision of an appropriate amount. Where there is a loss of the principal amount borrowed due to the collapse of the institution, the Council will seek legal and investment advice.

12. Security of Capital - the Creditworthiness Policy

12.1 Monitoring of credit ratings:

- The Council complies with the new CIPFA guidance on credit ratings.
- The Council uses the creditworthiness service provided by Sector Treasury Services. Data is provided on a weekly and daily basis. This service enables the Council to have access to ratings from all three credit rating agencies – Fitch, Moody's and Standards and Poor's as well as data which reviews market indicators. This is reviewed on an on-going basis for all investments and countries.
- If a counterparty's or investment scheme's rating is downgraded with the result that it no longer meets the Council's minimum criteria, the further use of that counterparty /investment scheme as a new investment will be withdrawn immediately;
- If a counterparty is downgraded but still meets the Council's minimum criteria, it would be watched closely and any further downgrading would result in the Council removing it from its lending list. It should however be noted that where the Council enters into a fixed term deposit, the borrower has no obligation to entertain any request for premature redemption, the Council may ask for the deposit to be broken. However this is not market practice and the institution is under no obligation to comply;
- If a counterparty is upgraded so that it fulfils the Council's criteria, its inclusion will be considered and put to the S151 Officer for approval; and
- The Council will continue its approach of investing no more than 25% of its aggregate funds to any particular counterparty or £15m whichever is higher. A detailed list of investment classification is included in Appendix B to this report.

12.2 Country Limits and Use of Foreign Banks

To ensure that the Council's investments are not concentrated in too few counterparties or countries, the Council will invest in strong UK and non UK foreign banks whose sovereign ratings meet its minimum criteria of A+ long-term Fitch credit rating (Moody equivalent A1 and Standards & Poor equivalent A+). No more than 25% of the Council's total aggregate funds will be invested in any one country apart from the UK. Sovereign ratings will remain at AAA.

12.3 Use of other Local Authorities

Where the investment is a straightforward cash loan the Local Government Act 2003 s13 suggests that the credit risk attached to English and Welsh local authorities is an acceptable one. The Council will limit its lending to local authorities in England and Wales.

12.4 Use of Multilateral Development Banks

S15 of the Local Government Act 2003 SI 2004 no. 534 amended provides regulations to clarify that investments in multilateral development banks were not to be treated as being capital expenditure. Should the Council invest in such institutions then only such institutions with AAA credit rating and government backing would be invested in consultation with the Council's treasury management adviser and the S151 Officer.

12.5 Use of Brokers

The Council deals with many of its counterparties directly through its daily dealings. From time to time the Council will use the services of brokers to act as agents between the Council and its counterparties when lending or borrowing. However no one broker will be favoured by the Council. The Council will ensure that sufficient quotes are obtained before investment or borrowing decisions are made via brokers.

13. Use of External Fund Managers

13.1 It is the Council's policy to use external fund mangers for part of its investment portfolio. The fund managers will use both specified and non-specified investment categories, and are contractually committed to keep the Council's investment strategy. The level of external balances is under constant review as the level of capital receipts diminishes. The performance of each manager is challenged quarterly by the S151 Officer or delegated officers and the Council's treasury advisers.

13.2 The Council currently uses two fund managers - Scottish Widows (SWIP) and Investec Asset Management. £40m of the Council's funds are currently managed on a discretionary basis by Investec and Scottish Widows.

In selecting the institutions to include in their counterparty listing, it is the external manager's policy to maintain a list of counterparties and assets based on the Council's set minimum criteria. This list is approved by their specialist credit team who independently research all potential counterparties before inclusion and regularly monitor and update to ensure that any change in credit worthiness and valuation is captured.

13.3 Both fund managers provide the Council with a periodic outlook on fund returns. For 2011/12, the worst case is 1.0%, and best case is 2.0%. These scenarios are based on the recent trend of the MPC rate which has continuously remained at 0.5% with predictions for a rate change in the next financial year.

13.4 Investec will continue to use other instruments like Floating Rate Notes and supranational bonds, in addition to gilts in order to increase returns of the portfolio. However they expect to see higher yield before establishing a position. Scottish Widows provide the Council with a forecast of their returns on the Council's investments based on the use of STL and GLF funds. The absolute return bond fund and the credit advantage fund may also be used in the course of the year if advantageous.

13.6 Pension Fund Cash

London Borough of Barking and Dagenham will comply with the requirements of The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009, which were implemented on 1January 2011, and therefore from 1 April 2011 will not pool pension fund cash with its own cash balances for investment purposes. This has therefore been reflected in future estimates of cash balances.

14. Reporting of Treasury management

14.1 At the end of the financial year, the Council will report on its investment and borrowing activities as part of the Annual Treasury Management Report and where necessary prepare a Mid-Year Treasury Management Report.

15. Other Implications

15.1 Risk Management - This report has risk management issues for the council. The risk that a counterparty could cease trading or risk that interest rates would fall adversely. The mitigation of these is contained in this report.

15.2 Contractual Issues - there are no direct contractual issues arising from this report.

15.3 Staffing Issues - there are no direct staffing issues arising from this report.

15.4 Customer Impact - there are no direct customer impact issues arising from this report.

15.5 Safeguarding Children - there are no direct safeguarding children issues arising from this report.

15.6 Health Issues - there are no direct health issues arising from this report.

15.7 Crime & Disorder Issues - This report has given careful consideration to the implications of Section 17 of the Crime and Disorder Act 1978 and there are no specific implications insofar as this report is concerned.

15.8 Property/Asset Issues – there are no direct property/asset issues arising from this report.

16 Background Papers Used in the Preparation of the Report:

Local Government Act 2003
CIPFA – Revised Prudential Code for Capital Finance in Local Authorities
CIPFA – Revised Treasury Management in the Public Services
Capital programme 2011/12 – 2014/15

17 List of Appendices:

Appendix A – Treasury Management Indicators 2011/12 – 2013/14
Appendix B – Investment Classification
Appendix C – Treasury Management Practices and Scheme of Delegation
Appendix D – Reporting Arrangements